Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
	)	
Connect America Fund	)	WC Docket 10-90
A National Broadband Plan for Our Future	)	GN Docket No. 09-51
Establishing Just and Reasonable Rates for Local Exchange Carriers	)	WC Docket No. 07-135
High-Cost Universal Service Support	)	WC Docket No. 05-337
Developing a Unified Intercarrier Compensation Regime	)	CC Docket No. 01-92
Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45
Lifeline and Link-Up	)	WC Docket No. 03-109

Declaration

Of

Susan M. Gately

On Behalf of

AdHoc Telecommunications Users Committee

August 24, 2011

DECLARATION OF SUSAN M. GATELY

TABLE OF CONTENTS

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
	)	
Connect America Fund	)	WC Docket 10-90
A National Broadband Plan for Our Future	)	GN Docket No. 09-51
Establishing Just and Reasonable Rates for Local Exchange Carriers	)	WC Docket No. 07-135
High-Cost Universal Service Support	)	WC Docket No. 05-337
Developing a Unified Intercarrier Compensation Regime	)	CC Docket No. 01-92
Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45
Lifeline and Link-Up	)	WC Docket No. 03-109

DECLARATION OF SUSAN M. GATELY

INTRODUCTION

I, Susan M. Gately, of lawful age, declare and say as follows:

1) My name is Susan M. Gately; I am President of SMGately Consulting, LLC (SMGC), 84 Littles Avenue, Pembroke, MA 02359. SMGC is a consulting firm specializing in telecommunications and public policy. I have participated in numerous proceedings before the Federal Communications Commission ("FCC" or "Commission") dating back to 1981 and have appeared as an expert witness in state proceedings before state public utility commissions. My Statement of Qualifications is annexed hereto as Attachment 1 and is made a part hereof.

2) I was asked by the AdHoc Telecommunications Users Committee to undertake a review and analysis of the specific areas identified below:

- Review the paper authored by Prof. Jerry A. Hausman of MIT that was submitted as Attachment 4 to the so-called "America's Broadband Connectivity (ABC) Plan" that is being sponsored by AT&T, Verizon and several other Incumbent Local Exchange Carriers ("ILECs"),[1] and to comment on his findings, conclusions and the specific quantitative analyses that he has presented therein specifically as they relate to consumer and economy-wide benefits of reducing intercarrier compensation rates.
- Review and analysis of the extent to which the Connect America Fund ("CAF") and the Advanced Mobility/Satellite Fund ("AMF") constructs proposed as part of the ABC plan will result in the distribution of USF funds for broadband deployment in a competitively neutral, technology agnostic manner that will support at most a single provider in most currently unserved or underserved areas.
- Respond to the Inquiries in the Further Notice of Inquiry related to the benchmark that would be used in the "Low Price Offset" proposed by AdHoc in its Initial Comments in response to the February NPRM.

[1] "America's Broadband Connectivity (ABC) Plan, Attachment 4 ("Consumer Benefits of Low Intercarrier Compensation Rates by Professor Jerry Hausman, MIT" (hereinafter "Hausman paper" or "Hausman")).

THE ECONOMYWIDE EFFECTS OF MISPRICING OF AN ESSENTIAL TELECOMMUNICATIONS INPUT

3) In 2007, the Ad Hoc Telecommunications Users Committee ("AdHoc") commissioned Economics and Technology, Inc. ("ETI") to prepare a study entitled "*Special Access Overpricing And the US Economy: How Unchecked RBOC Market Power is Costing US Jobs and Impairing US Competitiveness*."[2] I was one of the authors of that study. In it, ETI determined that "[i]n 2006, Bell company special access revenues exceeded $15.6-billion, generating some $5-billion in excess monopoly profits,"[3] and concluded that "[i]f a price reduction sufficient to bring the realized special access rates of return back to the FCC's last-authorized 11.25% level had become effective as of the beginning of 2007, the economywide benefit would be 95,000 additional jobs and $17.2-billion in additional GDP for 2007 alone."[4] Assuming that annual rate adjustments were made so as to maintain special access rates at the 11.25% "competitive" level, ETI estimated that "over the full 2007-2009 period ..., some 234,000 new jobs would have been created through the end of 2009, and the GDP gain for the three years combined would be in the range of $66-billion."[5]

---

[2] Lee L. Selwyn, Susan M. Gately, Helen E. Golding and Colin B. Weir, "Special Access Overpricing And the Us Economy: How Unchecked RBOC Market Power is Costing US Jobs and Impairing US Competitiveness," Economics and Technology, Inc., August 2007 ("ETI Study").

[3] Id., at 7.

[4] Id., at 15.

[5] Id. Of course, special access rates were not reduced in 2007 so as to maintain the last-authorized 11.25% rate-of-return, and in the years since 2007 special access revenues – and profits – have escalated to the point where they are now (assuming historic growth patterns in plant, expenses and revenues) generating something in excess of $10-billion in excess profits. Thus, were ETI's 2007 analysis to be replicated today, the deadweight loss in terms of competitive efficiency, jobs, and overall GDP growth would undoubtedly have increased competitive efficiency, jobs, and overall GDP growth would undoubtedly have increased commensurately with the escalation in aggregate excess special access prices and profits.

4) While the RBOCs challenged ETI's estimates of the economic impact of special access overpricing – and the FCC largely ignored it by steadfastly refusing to address the issue of special access rates altogether – the very same RBOCs have now come forward with the very same type of economic analysis to support their so-called "America's Broadband Connectivity (ABC) Plan." The ABC Plan, as its proponents describe it, "creates new universal service programs that explicitly support the provision of broadband service in high-cost areas, replacing the patchwork of legacy universal service programs that were designed to support plain old telephone service (POTS), ... reforms the intercarrier compensation system to reduce carriers' reliance on implicit support mechanisms that are no longer sustainable and were not designed to support the deployment of broadband, ... [and] eliminates obsolete regulations that are no longer necessary as carriers transition from POTS to IP-based broadband networks." Specifically, the proponents have commissioned a paper by Prof. Jerry A. Hausman of MIT to support the second of these three elements – *viz.*, "reform [of] the intercarrier compensation system to reduce carriers' reliance on implicit support mechanisms" embedded in existing switched access charges and other intercarrier payments.

> Under the [ABC] plan, the regulated terminating intercarrier compensation rates [including those that currently fall under the "switched access charge" regime] of all carriers except rate-of-return incumbent LECs are phased down to a uniform default rate of $0.0007 per minute by July 1, 2017.[6]

> The intercarrier compensation reform and universal service reform provisions of the ABC Plan are inextricably linked. Carriers are able to reduce their reliance on implicit support from intercarrier compensation because the plan provides support from new explicit

[6] ABC Plan, Attachment 1 "Framework of the Proposal," at 9.

mechanisms – the CAF and the access replacement mechanism.[7]

5) Prof. Hausman, in support of this specific proposal, "find[s] that a policy that sets a default rate for intercarrier compensation near zero would lead to significant gains in consumer welfare, as well as significant efficiency gains for the U.S. economy."[8] He explains that

> ... lower rates for all intercarrier compensation will lead to lower prices for consumers, added investment and innovation, or both ... Lower prices and added investment and innovation lead to increased consumer welfare and increased demand and increased output. Economic analysis demonstrates that lower costs are passed through to consumer prices at a minimum rate of 50%, even for a monopolist. However, as competition increases the percentage of pass-through approaches 100% (and can even be greater than 100%). Empirical economic studies typically find pass-through in competitive industries of approximately 100%, especially when the cost change is common to the entire industry.[9]

Of course, most US business, large and small, confront intense competition in their respective product and geographic markets and, in particular, face input cost conditions and input cost changes that are common to most or all firms in their respective industries. Prof. Hausman expects that "[n]early 100% of input cost reductions from lower intercarrier compensation rates ... would likely .. flow through to consumers and result in wireline and wireless price reductions, additional investment and innovation, or both." By direct analogy, it also follows that lower *telecommunications* costs to US businesses, operating in intensely competitive markets, would similarly "flow through to consumers and result in [economywide] price reductions, additional investment and innovation, or both." The effect would be

---

7 *Id.*

8 ABC Plan, Attachment 4 ("Consumer Benefits of Low Intercarrier Compensation Rates by Professor Jerry Hausman, MIT" (hereinafter "Hausman")), at para. 3.

9 Hausman, at para. 16, footnote references omitted.

multiplicative as US businesses flow through their lower telecommunications costs in their own output prices. Lower prices of consumer goods and services will result in increased disposable income, thereby permitting consumers to increase their spending in other economic sectors. Lower prices of capital goods and intermediate products and services will be flowed through in lower output prices by those businesses experiencing the now-reduced prices of their own essential inputs. In addition, lower *telecommunications* costs would increase the overall efficiency, productivity and competitiveness of US firms internationally, creating new jobs, new and increased exports, and a significant stimulus to the US economy and to growth in US GDP.

6) The 2007 ETI Study estimated that elimination of the then-$5-million in excess special access prices would, over just the initial three-year period, result in the creation of 234,000 jobs and $66-billion in GDP growth. Now, in 2011, I estimate that the level of excess special prices is in excess of $10-billion. Elimination of $10-billion deadweight loss would create nearly one-half million new jobs and grow the economy by more than $130-billion in the first three years alone as the lower costs of essential telecommunications services work their way throughout all economic sectors.[10]

[10] I estimate that ILEC total special access revenues for 2011 are between $22- and $25-billion. Assuming that about one quarter of those revenues represent services provided to wireless carriers alone – including those affiliated with the two largest RBOCs, AT&T and Verizon that would mean about $6-billion of the total represents a direct input cost to wireless service. Under that scenario, eliminating the excess profits from the special access payments made just by wireless carriers would reduce their operating costs by some $3-billion. Prof. Hausman anticipates a 100% flow-through of all reductions in wireless intercarrier compensation payments in the form of lower wireless prices. Hausman (at para. 22) estimates a per-subscriber monthly reduction in intercarrier compensation payments of $0.50, and that when spread over the 302-million US wireless subscribers, would produce $3.82-billion in consumer welfare gains. Extrapolating his calculation to wireless carrier special access payments, a $3-billion annual drop in special access charges applicable for wireless backhaul would translate into an additional $6.35-billion in wireless consumer welfare gains assuming, as Prof. Hausman has done here, 100% flow-through in the form of reduced wireless rates.

7) Consistent with the economic analysis presented in the 2007 ETI Study, Prof. Hausman similarly concludes that the conditions that result in welfare gains from reductions in input prices (intercarrier compensation charges in this case) operate symmetrically, in the opposite direction, if input prices are maintained at artificially high levels: "The opposite also is true; for example, if the Commission's policies that reduced rates for wireless were traffic were undermined, the result would be significant consumer welfare losses ..."[11] Precisely the same economic theory that argues for reductions in above-cost intercarrier compensation rates applies with equal strength to above-cost special access rates. Further delay in taking the required remedial measures is highly detrimental to the US economic and – particularly in light of the present and persistent economic downturn – is unconscionable public policy.

QUANTIFYING THE ECONOMIC EFFECTS OF PAST REDUCTIONS IN WIRELESS INTERCARRIER PAYMENTS

8) While Prof. Hausman is correct with respect to the economic theory supporting implementation of cost-based input prices and elimination of implicit support mechanisms, some of the quantitative estimates that he offers as to the effects of previous measures aimed at reducing intercarrier payments are superficial, exaggerated and certainly incomplete. According to his calculations, "[i]n part as a result of Commission policies reducing intercarrier compensation rates for wireless traffic, consumer surplus from 1996-2008 was approximately $115 billion per year ..." and "[f]rom 1996-2008, economic efficiency increase[s] ... produced an average annual gain in economic efficiency in this period of

[11] Hausman, at para. 3.

approximately $80.2 billion per year again in part as a result of Commission policies reducing intercarrier compensation rates for wireless traffic." If true, this would translate into $2.5-*trillion* in consumer surplus and efficiency gains over the thirteen year 1996-2008 period. Unfortunately this result is somewhat overstated.

9) Prof. Hausman has focused particular attention to the fact that the FCC's post-1996 policies with respect to intercarrier compensation were targeted at specifically benefitting the *wireless* industry ("Commission policies reducing intercarrier compensation rates for wireless traffic"), the practice resulted in pecuniary distortions across the various telecommunications technologies (wireline, wireless, VoIP) that actually worked to the detriment of those technologies that were not the beneficiaries of the Commission's largesse. One direct consequence of this technology-specific discriminatory treatment was that wireline services tended to be overpriced relative to wireless, thereby stimulating potentially uneconomic shifts from the former to the latter. Long distance calling was particularly hard-hit by this disparity in intercarrier compensation treatment. Wireless carriers, freed from the requirement to pay switched access charges for most wireless-to-wireline long distance calls, simply stopped charging extra for long distance calling, effectively creating a nationwide "local calling area" for their customers. That policy, coupled with block-of-use pricing, "free" night/weekend calling and "free" mobile-to-mobile calling, made many long distance calls truly free of charge – particularly for residential wireless users. It is hardly surprising that consumers shifted large portions of their long distance calling to their wireless phones – at a far greater

rate than the outright "cutting the cord" type of substitution of wireless for wireline.[12]

10) An *indirect* effect of the FCC's nurturing attitude toward wireless was that the shift of long distance calling away from wireline reduced the volume of ILEC billable switched access minutes – and revenues. Switched access minutes peaked in 2000 at 566.9-billion; by 2008 (the most recent year for which this data is available) the volume had plummeted to 315.7-billion.[13] Extrapolating that trend beyond 2008 would suggest a 2011 switched access volume of only about 225-billion minutes. Over a similar period (2000-2009), total *wireless* minutes of use skyrocketed from 335.0-billion in 2000 to 2.32-*trillion* in 2009.[14] ILEC complaints that the inclusion of implicit support within switched access is "unsustainable" going forward is, in large part, a direct consequence of the FCC's policy of coddling certain technologies at the expense of others.[15]

11) In addition to ignoring the cross-elastic effects of consumer substitution of

[12] FCC statistics do not distinguish between wireless "local" and "toll" usage as these concepts are understood in the wireline world. However, for 2008, 30% of all wireless minutes were reported as interstate, 68% were intrastate, and the jurisdiction for the remaining 2% was indeterminate. Since most interstate calls would be "toll" if placed from a wireline phone and a large proportion of intrastate calls would also be "toll" as well, an estimate of wireless "toll" usage (both inter- and intrastate) of about of 40% of total wireless minutes would not be unreasonable and, if anything, likely conservative. See FCC *Trends in Telephone Service*, September 2010, at Table 11.4.

[13] *Id.*, at Table 10.1; 15th CMRS Report, at Table 14 and Chart 19..

[14] If we assume that 40% of the 2.32-trillion total wireless minutes in 2009 would have been "toll" calls under the wireline toll definition, then somewhere in the range of what would have been 900-billion ILEC switched access minutes of use in 2009 were diverted to wireless.

[15] It is perhaps noteworthy that, to the best of my recollection, no RBOC has ever complained about the preferential treatment being afforded wireless carriers with respect to switched access these same companies are constantly complaining about "the refusal of many interconnected VoIP service providers to pay access charges" [NPRM, at fn. 719, citing OPASTCO Comments in re NBP #19 at 22 (filed Dec. 7, 2010)]. There is, of course, a simple explanation for this obvious inconsistency in the RBOCs' position – the two largest RBOCs, AT&T and Verizon, control the two largest wireless carriers, AT&T Mobility and Verizon Wireless. Neither AT&T nor Verizon have any consequential involvement in the "interconnected VoIP" business, and thus view this technology as cannibalizing their embedded circuit-switched customer base and revenues.

wireless for wireline long distance calling due to the disparate access charge treatment afforded these two technologies, Prof. Hausman also appears to have ignored the own-price elasticity of wireless service in making his "consumer welfare" and "consumer surplus" calculations. According to Prof. Hausman, "over the period 1996-2008 the increase in consumer surplus for cellular usage totaled approximately $64.50 per month or $774 per year per cellular subscriber. In total the gain in consumer surplus was approximately $114.5 billion per year over the period using the average number of subscribers of approximately 148 million nationwide over the period."[16] His calculation of the increase in consumer surplus appears to be premised upon the notion that, but for the FCC's wireless intercarrier compensation policy and perhaps other unspecified factors affecting wireless price levels, each of the (average of) 148-million consumers would have paid $64.50 more per month of the entire 1996-2008 period. That assumption requires that even at a price that was $64.50 higher than that actually being charged, all of those same 148-million consumers would have subscribed for the (considerably higher priced) wireless service and used their wireless phones for the same number of minutes even at the (considerably higher) average price per minute that would have been in effect had those policies (and other unspecified factors) not been in effect or operative.

THE ABC PLAN'S PROPOSED REFORMATION OF INTERCARRIER COMPENSATION RATES

12) Moreover, nowhere in Prof. Hausman's attempt to quantify the effects of the ABC

[16] Hausman, at para. 11, footnote references omitted.

Plan's proposed ICC revisions did he address or consider the detrimental effect upon consumer welfare associated with the proposed offsetting *increases* in explicit support mechanisms that would arise to offset, if not dollar-for-dollar at least partially, the access charge reductions. The ABC Plan basically calls for a "make whole" policy whereby implicit support currently produced via access charges or other intercarrier compensation would be offset, dollar-for-dollar, by explicit support payments inuring to the same ILECs. While the net effect of these shifts from implicit support via usage-sensitive access charges to explicit support via some type of fixed surcharge is likely to still produce consumer welfare gains and contribute to overall economic efficiency (because the price elasticity of usage is greater than that for access to the public telecommunications network) the net effect will likely be much smaller than that predicted by Hausman *if the FCC accepts the "make whole" principle being advocated by the ILECs*. Of course, as AdHoc has suggested on numerous occasions in the past,[17] there is no inherent reason why such claimed ILEC make whole entitlement should be adopted and, indeed, Prof. Hausman's failure to consider any of such a policy's detrimental effects should not be overlooked.

13) A most troubling aspect of the ABC Plan calls for interconnected VoIP traffic to become subject to switched access charges beginning in January 2012.[18] Other than

[17] See for example Ad Hoc's Initial Comments filed on April 18, 2011 at 49 – 64 in *Connect America Fund, et al,* WC Docket Nos. 10-90, 07-35, 05-337, 03-109, CC Docket Nos. 01-92, 96-45, GN Docket No. 09-51, Notice of Proposed Rulemaking and Further Notice of Proposed Rulemaking, 26 FCC Rcd 4554 (2011) ("NPRM").

[18] ABC Plan, Attachment 1, at 10: "... effective January 1, 2012 ... VoIP ... traffic will be rated at interstate access rates if the call detail indicates an "access" call, or at reciprocal compensation rates if the call detail indicates a "non-access" call. All "toll" traffic that originates in IP or terminates in IP will be subject to current interstate access rates (regardless of whether it is interstate or intrastate)." Footnote references omitted.

supporting the parochial interests of the RBOCs and their wireless subsidiaries, there is no justification for maintaining the discriminatory favorable treatment of wireless while pushing interconnected VoIP into "parity" with traditional circuit-switched services. The correct solution is to achieve parity by moving all intercarrier rates to technology-neutral cost-based levels, not to preserve the advantageous treatment being afforded RBOC-affiliated wireless carriers while undermining the ability of RBOC-threatening interconnected VoIP providers to develop their nascent technology and in so doing to challenge the RBOCs' dominance of both wireline and wireless services.

14) Finally, throughout his paper, Prof. Hausman makes numerous references to "near zero" ICC rates while never actually defining precisely what "near zero" means. As presented in the ABC Plan, "near zero" translates into a terminating intercarrier charge of $0.0007 per minute – the same level that has been applied since 2001 for ISP-bound dial-up traffic.[19] However, the relationship between a $0.0007 ICC rate and the underlying *cost* of terminating inbound calls has never been established. AdHoc has consistently advocated *cost-based* access charges and local intercarrier rates. Above-cost rates distort economic and technology decision-making and produce inefficient outcomes – particularly where they create artificial barriers to competition. Similarly, *below-cost* ICC rates will produce similar inefficient and anticompetitive results, albeit in the opposite direction. The Commission needs to confront this issue both with respect to switched services as well as with respect to special access.

[19] *Intercarrier Compensation for ISP-Bound Traffic*, CC Docket Nos. 96-98, 99-68, Order on Remand and Report and Order, 16 FCC Rcd 9151 (2001) (*ISP Remand Order*); *remanded but not vacated by WorldCom, Inc. v. FCC*, 288 F.3d 429 (D.C. Cir. 2002

Further delay – and continued arbitrary and uneconomic treatments – is not in the public interest or in the interest of the US economy overall.

TARGETTING $2.2-BILLION IN CAF FUNDS TO PRICE CAPS AREA IS NEITHER COMPETIVELY NOR TECHNOLOGICALLY NEUTRAL

15) The ABC Plan would allot $2.2-billion in CAF dollars to be spent in areas presently served by incumbent price cap carriers in a manner that is facially similar to one of the two CAF distribution alternatives put forth by the Commission in the NPRM: the use of a forward-looking economic cost (FLEC) model in conjunction with a the grant of a right of first refusal (ROFR) to the incumbent carrier.[20] The ABC Plan leap-frogs the FCC's decision making process, proposing a full-blown solution set premised upon one of the two alternative CAF distribution proposals identified in the NPRM in advance of a decision by the Commission based upon the thousands of pages of comments already received in the record.

16) Not only does the ABC Plan presuppose the decision as to the best CAF disbursement methodology (the framework of the new USF plan) it then populates the framework with the dollar amounts, thresholds, and models of its liking. In the February NPRM the Commission queried whether it made sense to implement CAF disbursements on a different time track than disbursements for RLECs, and if so whether it should designate a specific portion of the overall CAF budget to price cap serving areas, and if so how it should

[20] ABC Plan, Attachment 1 at 6 and *USF / ICC Transformation NPRM, 26 FCC Record at 4681-90, paras 417-447.*

go about determining how much of the CAF budget should be designated for that purpose.[21] The ABC plan skips the preliminary questions of *whether* there should be a prices caps area set aside and *how* such a set-aside should be sized instead predetermining that $2.2-billion of the $4.5-billion in future CAF disbursements would be limited to use for households located in the service areas of the price caps carriers and by structuring the plan such that they have first dibs on the more than 80% of those dollars. By their own reckoning the incumbent price caps ILECs, primarily as a result of thresholds and cost model they have incorporated it the plan, would have a right of first refusal for $1.8-billion (82.2%) of those $2.2-billion dollars – guaranteeing them a right of first refusal for almost $1.80 for every $1.00 USF dollar flowing to those same carriers today.[22] Moreover, while the Commission queried in the NPRM whether it would be appropriate to utilize a forward looking economic cost model as part of the distribution mechanism and sought comments upon the best approach (scorched node versus Greenfield, DSL versus FTTP, appropriate geographic unit)[23] the ABC plan contains a fully formed plan developed using the approach its authors, not the FCC deemed best and limiting the costs included in the FLEC model to those for wireline services only rather than for all potential technology options (e.g., wireless (fixed and mobile) and satellite).

17) Review of the RLEC and ABC plan proposals for distribution of CAF dollars has only served to put more clearly into focus the need for the Commission to implement a

---

[21] The NPRM sought comment on whether it made sense to start CAF distributions with price caps areas and if so how to divide the CAF funds *USF / ICC Transformation NPRM, 26 FCC Record* at 4684 and 4689 at paras 430 and 447.

[22] USAC 2010 disbursements to Price Caps Carriers were reported at approximately $1-Billion, *USF / ICC Transformation NPRM* at page 58.

[23] *USF / ICC Transformation NPRM, 26 FCC Record* at 4685 to 4687, paras 432 to 438.

competitive mechanism for fund distribution to ensure the most broadband deployment for the lowest level of funding rather than give into the parochial and self-serving plans being circulated by the incumbent carriers.

18) The compromise reform proposals submitted by the price caps and rate of return carriers walk away almost entirely from reverse auction option the Commission had been contemplating and instead propose plans that would guarantee that the lion's share of all CAF dollars available to stimulate broadband would go to incumbent LECs.

19) Record evidence to support designating a specific portion of the overall CAF funding level to a particular carrier, class of carrier or technology choice would need to demonstrate that specific choice to offer the most cost effective method of getting broadband deployed to unserved and underserved households. In other words the only record that would support such a pre-designation would be one that demonstrated that more households that have no adequate broadband option available today would have broadband deployed to them as a result of that designation than if the technology, carrier, or carrier class determination were not hard-wired. At this point there is no record evidence that supports giving the price caps LECs the right of first refusal (aka, guaranteed availability) to $1.8-billion of CAF funds. There is no record evidence that continuing to subsidize rate of return carriers at the same levels they receive today will ensure more widespread broadband availability in the future. There is no record evidence to support designating $2.2-billion of CAF funds to wireline broadband deployment in the areas served by price caps carriers. No record evidence that the use of wireline technology across the price caps carriers regions will result in more broadband deployment than the use of a mixture of wireline and non-wireline technologies.

20) In fact the strongest evidence in the record suggests just the opposite. ViaSat, in both its initial comments and later expartes to the Commission indicates that if sufficient CAF funds are made available satellite providers will be incented to launch additional satellites to provide broadband service to that 40% of the US population that will not already have broadband satellite service available to it following the scheduled launch of the VIASAT-1 next month. In those same documents the costs of expanding satellite capacity and making broadband satellite service at a minimum of 4/1 Mbps to 3.3 million additional households (not limited to price caps or rate of return carrier territories) was reported as $1.8-billion.[24]

21) Analysis of the metrics associated with the $300 AMF component of the ABC plan suggests that the plan's proponents may also believe that satellite service may be a more cost effective alternative. The RLECs propose designating $2.2-billion in CAF funds for the deployment of broadband service to 2.2-million subscribers based upon a modeling of wireline costs (approximately $1,000 per subscriber). At the same time the plan proposes setting aside $300-million in AMF funding to deploy service to 730-thousand of the highest cost subscribers. The plan is silent as to whether all or some large or small portion of those highest costs households are anticipated to actually receive broadband under its plan as constructed, but the expectation that deploying service by some method other than wireline service is more cost effective is inherent in the proposal.

22) Per the ABC plan and RLEC plans all but the most costly connections (those the incumbent carriers have no interest in providing) will be provided over wireline connections

[24] ViaSat Comments at 16.

by the very incumbent carriers that have heretofore failed to deploy broadband to those customers and virtually all non-wireline technology options and non-incumbent carriers will be denied from competing for those CAF dollars with innovative and perhaps more efficient broadband options. In the words of ViaSat:

> It would be extremely difficult for satellite providers to raise such capital if the CAF skews competition by precluding full and direct satellite participation while at the same time subsidizing less-efficient, higher-cost terrestrial competitors. This would not only harm consumers, but also could damage the ability of satellite providers to provide service for critical applications—including first responder, public safety, law enforcement, and military applications.[25]

23) The ABC plan for distribution of CAF dollars would be hardwired for $2.2-billion in annual CAF funds for each of the next 10 years to wireline carriers to use in deploying service in the price caps carriers service areas. The plan's proponents describe it as "technology neutral"[26] because after the wireline carriers are awarded the $2.2-billion in CAF dollars each year based upon the COSTQUEST modeled costs of a wireline broadband network, they will in fact be free to utilize those funds to deploy some other more efficient non-wireline broadband technology should one be available. If this is indeed to be viewed as some form of technology neutrality, it is a most perverted form.

24) The most obvious problem is that the proposed plan does not appear to include any mechanism that will keep the price cap LECs from simply flowing the differential between the CAF dollars granted on the basis of the wireline cost model and the cost of deploying a more cost-effective technology to any place but their shareholders and their

[25] Initial Comments of ViaSat at footnote 10.

[26] The ABC "Framework" states: "The broadband service obligation is technology-neutral: providers can use any wireline or wireless technology that meets the specified bandwidth and service requirements." at 3.

bottom line. Also not clear from the plan is how wireline ILECs, with no wireless spectrum and no satellites, would in fact utilize alternate technologies – unless they intend to act as intermediaries purchasing broadband connections from alternative technology providers that have been shut out of the $2.2-billion allocated for wireline carriers and keeping the difference in price.

25) More importantly, although the ABC Plan doesn't preclude carriers from using any portion of the $2.2-billion being set-aside for wireline carriers from using alternate technologies that may be more cost-effective, it denies those end users that ultimately pay the USF subsidies as surcharges on their telecommunications bills the benefits of those potentially lower-cost technologies. It also means that broadband deployment will not occur for as many customers as it would have if the funds were distributed based upon the most economically efficient technology choice – not a carrier-designed wireline-only cost model.

AD HOC'S PROPOSED "LOW PRICE OFFSET" SHOULD BE IMPLEMENTED AS PART OF THE "NEAR TERM REFORMS" DESIGNED TO MAKE CAF BROAFBAND FUNDS AVAILABLE

26) In its attempt to ensure that those high cost fund dollars flowing to carriers today are in fact necessary for the provision of universal service in conjunction with its desire to begin to make funds being used by the present HCF portion of the USF fund available to ensure greater broadband deployment through the new CAF the FCC proposed a number of "near-term" reforms in the NPRM. In conjunction with those proposals AdHoc suggested the FCC implement a "low price offset" to carriers' current USF disbursements for those carriers whose local service prices are below a relevant benchmark level thereby eliminating interstate

subsidization of low cost intrastate services. The Further Inquiry requests comments upon that proposal and what the relevant benchmark rate might be, whether the benchmark should ratchet up over time, and whether the same benchmark should be used for ICC purposes.

27) In setting the benchmark rate to be used as the "low price offset" the 96 Act's requirement that universal service be available at "affordable" and "reasonably comparable" prices is a useful guidepost. The theory behind the offset is that any ILEC that is receiving USF subsidies while at the same time charging less than the average price for the local service (either of its own choice because it is deregulated or as a result of some state regulatory constraint) by definition does not need its full USF subsidy because it could raise local rates to at least the average level paid by subscribers in the rest of the country. The Further Notice postulates using the "average" local service price (with fees) reported in the 2008 Reference Book of rates as a benchmark,[27] and AdHoc believes that average rate represents a perfectly valid benchmark.

28) The average rate of $15.62 ($21.36 with SLCs and fees) quoted in the Further notice is an average for residential flat rate service based upon a nationwide sample of 95 cities.[28] The 2008 Reference Book of Rates also contains an average residential measured service price of $8.49 ($17.29 with SLCs and fees) for those 79 sample cities where measured residential service is also available – the differential between the measured service average price and the measured service price offered by the low cost service provider would be

[27] Public Notice at 7.

[28] Industry Analysis and Technology Division. Wireline Competition Bureau, *Reference Book of Rate, Prices Indicie, and Household Expenditures for Telephone Service,* at Table 1,1 (2008).

appropriate for the carriers offering measured service. Those incumbent LECs whose subscribers purchase service as part of a bundled service offering (including some combination of local, intra and interstate long distance, features and functions, internet access of anything else) would be required to report the disaggregated price for the local service portion of the offering. Although the incumbent local service providers in many jurisdictions have been deregulated[29] the vast majority still remain subject to some kind of tariffing requirement.

29) As an alternative (one also identified in AdHoc's initial comments) the Commission could also utilize the highest rate presently applicable (with fees) for comparable service in a given state. Even the highest rate paid by other local service customers in the same state is by definition both "affordable" (or customers would not be purchasing the service) and "reasonably comparable." If the FCC views the gathering of such state by state local service pricing as too onerous it could instead rely upon the individual sample city data found in the 2008 Reference Book. Table 1.3 in that document contains both flat and measured rate prices for sample cities in 42 of the 50 US states – the FCC could utilize the highest sample rate from each state in that document, leaving it with the task of gathering pricing information only for the 8 remaining states and US territories not included in the state-specific results.

[29] See AdHoc Comments in this proceeding filed April 18, 2011 at 29 and Appendix A, Declaration of Susan M. Gately at pp 8 – 10 and Exhibit 15.

VERIFICATION

The foregoing statements are true and correct to the best of my knowledge, information and belief.

Susan M. Gately

Attachment 1

Susan M. Gately
Statement of Qualifications

Susan M. Gately founded SMGately Consulting, LLC (SMGC) in January of 2011. Susan is an economic and policy expert specializing in the telecom arena with more than thirty years of consulting experience. Her specific experience lies in the areas of

- Telecom industry structure;
- Regulatory regimes;
- Cost development;
- Pricing and rate structure; and
- Telecom services and network management practices.

Prior to founding SMGC Susan was a partner in and the Senior Vice President at Economics and Technology, Inc (ETI) providing advising, litigation support, expert testimony, white papers, and in-house training and education to ETI's myriad carrier, governmental agency and large business clients. Susan has provided expert testimony on a variety of telecom policy matters and participated in hundreds of FCC proceeding on access charges, universal service, separations and cost accounting, and form of regulation.

Ms. Gately has devoted a lot of her time over the last several years to researching and analyzing conditions extent in the wireline and wireless telecommunications markets in the US, the conditions that have led to the current market structures and the implications for users of those networks. Among the work codifying the research are the following papers released in 2010. *Regulation, Investment and Jobs: How Regulation of Wholesale Markets Can Stimulate Private Sector Broadband Investment and Create Jobs* (With Helen E. Golding, Lee L. Selwyn and Colin B. Weir. Released in February, 2010.) *Revisiting US Broadband Policy: How Reregulation of Wholesale Services Will Encourage Investment and Stimulate Competition and Innovation in Enterprise Broadband Markets* -- (With Helen E. Golding, Lee L. Selwyn and Colin B. Weir. Released in February, 2010.) *Longstanding Regulatory Tools Confirm BOC Market Power: A Defense of ARMIS* (With Helen E. Golding, Lee L. Selwyn and Colin B. Weir. Released in January, 2010.)

Susan has been involved in the analysis of incumbent LEC intrastate and interstate access tariffs since the inception of the tariffs in 1984. She has participated in virtually every major FCC proceeding on access charges and price caps, and is among the nation's leading experts on access charge rate structure, methodology, and policy. Ms. Gately has designed and presented training sessions for corporate users and public service commission staffs in subject areas ranging from

tariff structures, universal service, contract negotiation strategies, regulatory practices, and in-depth exploration of public policy issues.

Ms. Gately has also been extensively involved in the analysis of cost and operational data submitted by telephone companies in the context of regulatory proceedings and audits, including the submission of expert testimony in state public utility proceedings. Her responsibilities have involved the analysis of telephone company cost data and cost study methodologies. Ms. Gately's work has included the development of alternative cost figures for the purpose of presenting alternative rate proposals. She has participated in the preparation of expert testimony on local calling area expansion, affiliate transactions, survey and statistical methodologies, cost study methodologies, revenue requirement, infrastructure and modernization, new service pricing, access pricing, unbundled network element pricing, avoided retail costs for use in setting wholesale prices and other issues related to the opening and operation of markets.

Ms. Gately has devoted a large amount of time to the analysis of the Interstate Access Tariffs (to non-price issues as well as the more traditional cost and rate questions) since the filing of the initial access tariffs in 1983. Ms. Gately has participated in the preparation of hundreds of submissions to the FCC on issues including access service pricing and rate structures, price caps implementation, access service costs (including cost allocation of regulated and non-regulated services), and alternative forms of regulation. Among those issues recently addressed at the FCC has been the appropriate rate structure for the collection of universal service costs from end users, and rules related to the level of universal service funding that should be available to rural telecommunications service providers. Ms. Gately was also actively involved in the investigation of the level of cost to be recovered from the implementation of local number portability (LNP) and the appropriate method of recovering those costs. Ms. Gately was also involved in modeling and analysis of the FCC's last major revision to its access charge and price caps plan — the so called "CALLS" plan.

Throughout 1994, acting as a staff expert for the Delaware PSC Staff, Ms. Gately participated actively in the litigation of rules implementing an alternative regulatory plan put in place by the Delaware state legislature. Ms. Gately was one of the designated staff negotiators during an attempted negotiated settlement of the rules using Alternate Dispute Resolution (ADD) techniques. Subjects addressed by the PSC's Rulemaking included, among other things, the development of both incremental and fully distributed costing methodologies to be used by Bell Atlantic for use as incremental cost floors, and to ensure against cross-subsidization. She co-authored comments on behalf of staff regarding cost methodology, rate imputation, and unbundling requirements.

Ms. Gately was particularly active in the examination of ILEC cost data and deployment plans for basic rate interface (BRI) ISDN service. Ms. Gately was involved in all facets of a New England Telephone BRI ISDN investigation that culminated in an affordable, widely deployed ISDN offering in Massachusetts. She has also prepared and/or sponsored testimony and comments relative to the deployment and pricing of ISDN services in Colorado, Tennessee, Texas, Ohio, and Connecticut. Ms. Gately also co-authored two separate ISDN position papers in conjunction with Dr. Lee L. Selwyn; *A Migration Plan for Residential ISDN* for the Electronic Frontier Foundation and *The Prodigy ISDN White Paper: ISDN Has Come of Age* for Prodigy Services Company.

Ms. Gately was also heavily involved in the development of avoided cost estimates for use in setting wholesale prices in a resale environment. Ms. Gately co-authored (with Dr. Lee L. Selwyn) *Commercially Feasible Resale of Local Telecommunications Services: An Essential Step in the Transition to Effective Local Competition.* She has participated in resale proceedings and or inter¬connection arbitrations (relative to wholesale pricing) in California, Hawaii, Illinois, Ohio, Nevada, and Louisiana.

Ms. Gately was also involved in the analysis of issues related to the application of several of the Bell Companies for Section 271 authority to enter the interLATA long distance market. Ms. Gately has also undertaken a detailed analysis of the Continuing Property Record (CPR) audits conducted by the Accounting and Audits Division of the FCC. That analysis culminated in the preparation of a paper (written in conjunction with Dr. Lee L. Selwyn) *Inflated BOC Prices: An Agenda for State PUC Actions Arising from the FCC CPR Audits.*

Ms. Gately has assisted numerous Fortune 100 companies in the evaluation of pricing, terms and conditions as part of the long distance and local procurement process.

In addition to her regulatory work, Ms. Gately has been a frequent speaker at various industry gatherings including large conventions and more specialized seminars and conferences. The subject matters have included the following wide range of issues:

- Negotiation of custom network contracts;
- ILEC central office collocation;
- The FCC's price cap plan for ILECs;
- Principles for pricing ISDN basic rate service.
- USF Funding for wireless CETCs
- Reformation of the USF High Cost Fund

Ms. Gately has co-authored a number of papers of note not mentioned above. Specifically, Ms. Gately was co-author (and project manager) of a report authored jointly by ETI and Hatfield Associates, Inc. entitled: *The Enduring Local Bottleneck: Monopoly Power and the Local Exchange Carriers.* She also managed and co-authored (with Dr. Lee. L. Selwyn) *Access and Competition: The Vital Link* (submitted to the FCC in support of a petition by the Ad Hoc Telecommunications Users Committee requesting initiation of combined access charge and separation reform proceeding) as well as a paper entitled *LEC Price Cap Regulation: Fixing the Problems, Fulfilling the Promise* (co-authored with Dr. Lee L. Selwyn, Dr. David J. Roddy, Scott C. Lundquist and Sonia N. Jorge) filed in support of the Ad Hoc Telecommunications Users Committee's comments in the FCC's Docket 94-1 review of the LEC Price Caps Plan. Ms. Gately also co-authored *The "Connecticut Experience" with Telecommunications Competition: A Case in Getting it Wrong* , with Lee L. Selwyn and Helen E. Golding. Ms. Gately's most recent work, *Lost in Translation: How Rate of Return Regulation Transformed the Universal Service Fund for Consumers into Corporate Welfare for the RLECs,* co-authored with Scott C. Lundquist was completed and filed in support of Western Wireless Corporation's 2003 Petition to the FCC to calculate USF funding requirements on a forward look cost basis.

Prior to joining ETI, Ms. Gately was employed as an Economic Analyst at Systems Architects, Inc. Her work there primarily involved the analysis of economic data and survey results for the Health Care Finance Administration, the Social Security Administration, and the Department of Defense.

Susan has a Bachelor of Arts degree in Economics from Smith College (1980).

Appearances in Regulatory Proceedings

Telecommunications Regulatory Board of Puerto Rico , *Telefónica Larga Distancia de Puerto Rico, Inc., Petition for arbitration pursuant to Section 47 U.S.C. 252 (b) of the Federal Communications Act and Section 5 (b), Chapter III, of the Puerto Rico Telecommunications Act, regarding interconnection rates, terms and conditions with Puerto Rico Telephone Company, Inc.*, Docket No. JRT-2006-AR-0001, on behalf of Telefónica Larga Distancia de Puerto Rico, Inc., Direct Testimony filed January 16, 2007, Reply Testimony filed February 7, 2007, cross-examination February 14, 2007, Declaration filed March 30, 2007.

United States District Court, District of New Jersey, in *Re: AT&T Corp. v. JM Telecom, LLC,* Civil Action No. 99-2578, on behalf of AT&T Corp., Expert Report filed December 5, 2003.

California Public Utilities Commission, in *Re: Order Instituting Rulemaking to Review Policies Concerning Intrastate Carrier Access Charges*, Docket No. R.03-08-018, on behalf of AT&T Communications of California, Inc. , Declaration filed November 12, 2003.

Colorado Public Utilities Commission, in *Re: Application of US West Communications, Inc. for Investigation into Switched Access Rates*, Docket No. 00A-201T, on behalf of AT&T Communications of the Mountain States, Inc., Testimony of Lee L. Selwyn, filed July 18, 2000, adopted by Susan M. Gately, cross-examined on October 17, 18, 2000.

Arizona Corporation Commission, in *Re: In the Matter of the Application of US West Communications, Inc., a Colorado Corporation, for a Hearing to Determine the Earnings of the Company, the Fair Value of the Company for Ratemeking Purposes, to Fix a Just and Reasonable Rate of Return Thereon and to Approve Rate Schedules Designed to Develop Such Return*, Docket No. T-1051B-99-105, on behalf of AT&T Communications of the Mountain States, Direct Testimony filed August 9, 2000, Supplemental Direct Testimony filed November 13, 2000.

United States District Court, District of Massachusetts, in *Re: Telephone Management Corporation, Plaintiff, v. State Street Bank and Trust Company, Defendant*, Civil Action No. 97-10993 PBS, on behalf of State Street Bank and Trust Company, Expert Report filed July 17, 1998.

Delaware Public Service Commission, in *Re: In the Matter of Development of Regulations for the Implementation of Telecommunications Technology Investment Act*, Docket No. PSC Reg. 41, on behalf of Delaware Public Service Commission Staff, cross-examination March 2, 1995.

New York Public Service Commission, in *Re: Proceeding on Motion of the Commission to Investigate Performance-Based Incentive Regulatory Plans for New York Telephone Company*,Docket No. 92-C-0665, on behalf of Cable Television Association of New York, Supplemental Testimony filed September 8, 1994.

California State Legislature, in*Re: California Long Distance Telecommunications Consumer Choice Act*, Assembly Bill 3720, on behalf of AT&T, Statement before the California State Legislature, April 11, 1994.

Tennessee Public Service Commission, in*Re: In the Matter of the Commission's Investigation of Integrated Services Digital Network (ISDN)*, on behalf of Prodigy Services Company, oral testimony, November 11, 1992.

Arizona Corporation Commission, in *Re: In the Matter of the Commission's Examination of the Rates and Charges of the Mountain States Telephone and Telegraph Company* , Docket No. E-1051-88-306, on behalf of Residential Utility Consumer Office, Direct Testimony filed July 13, 1990, Rebuttal Testimony August 7, 1990.

Papers and Reports

Regulation, Investment and Jobs: How Regulation of Wholesale Markets Can Stimulate Private Sector Broadband Investment and Create Jobs (With Helen E. Golding, Lee L. Selwyn and Colin B. Weir. Released in February, 2010.)

Revisiting US Broadband Policy: How Reregulation of Wholesale Services Will Encourage Investment and Stimulate Competition and Innovation in Enterprise Broadband Markets- (With Helen E. Golding, Lee L. Selwyn and Colin B. Weir. Released in February, 2010.)

Longstanding Regulatory Tools Confirm BOC Market Power: A Defense of ARMIS (With Helen E. Golding, Lee L. Selwyn and Colin B. Weir. Released in January, 2010.)

The Role of Regulation in a Competitive Telecom Environment: How Smart Regulation of Essential Wholesale Facilities Stimulates Investment and Promotes Competition (With Lee L. Selwyn, Helen E. Golding, Susan M. Gately, and Colin B. Weir. Released in March, 2009.)

Special Access Overpricing and the US Economy: How Unchecked RBOC Market Power is Costing US Jobs and Impairing US Competitiveness (with Lee L. Selwyn, Colin B. Weir, and Helen E. Golding) Economics and Technology, Inc., prepared on behalf of the AdHoc Telecommunications Users Committee, August 2007.

HOLD THE PHONE: Debunking the Myth of Intermodal Alternatives for Business Telecom Users In New York, prepared on behalf of the UNE-L CLEC Coalition in New York, August 2005.

*The 2005 Update of the 1999 TFP Model Calculating a Productivity Factor for Interstate Special Access***,** prepared on behalf of the Ad Hoc Telecommunications Users Committee**,** submitted as an attachment to Susan M. Gately's Reply Declaration, filed in FCC WC Docket No. 05-25, *Special Access Rates for Price Cap Local Exchange Carriers*, July 29, 2005.

Striking a Nerve: ETI's Rejoinder to the NTCA/OPASTCO False Premises Report, (with Lee L. Selwyn and Scott C. Lundquist) prepared on behalf of Western Wireless, October 2004.

Competition in Access Markets: Reality or Illusion, A Proposal for Regulating Uncertain Markets, (with Lee L. Selwyn and Helen E. Golding), prepared on behalf of the Ad Hoc Telecommunications Users Committee, August 2004.

Lost in Translation: hoe Rate of Return Regulation Transformed the Universal Service Fund for the Consumers into Corporate Welfare for the RLECs, (with Scott C. Lundquist) prepared on behalf of Western Wireless, February 2004.

Business Telecom Users Benefit from UNE-P Based Competition, (with Lee L. Selwyn) prepared on behalf of AT&T, January 2003.

Inflated BOC Prices: An Agenda for State PUC Action Arising from the FCC CPR Audits, (with Lee L. Selwyn) prepared on behalf of AT&T, July 2000.

The "Connecticut Experience" with Telecommunications Competition: A Case Study in Getting it Wrong, (with Lee L. Selwyn and Helen E. Golding) prepared on behalf of AT&T, February 1998.

Commercially Feasible Resale of Local Telecommunications Services: An Essential Step in the Transition to Effective Local Competition, (with Lee L. Selwyn) prepared on behalf of AT&T, July 1995.

The Enduring Local Bottleneck: Monopoly Power and the Local Exchange Carriers,prepared by Economics and Technology, Inc. (with Lee L. Selwyn) and Hatfield Associates, Inc., on behalf of AT&T, MCI Communications Corporation, Competitive Telecommunications Association, February 1994.

LEC Price Cap Regulation: Fixing the Problems and Fulfilling the Promise , (with Lee L. Selwyn, David J. Roddy, Sonia N. Jorge and Scott C. Lundquist), prepared on behalf of the Ad Hoc Telecommunications Users Committee, May 1994.

Access and Competition: the Vital Link, (with Lee L. Selwyn), prepared on behalf of the Ad Hoc Telecommunications Users Committee, April 1994.

Pricing and Policy Issues Affecting Local/Access Service in the U.S. Telecommunications Industry, (with Lee L. Selwyn, W. Page Montgomery, and Jenny H. Yan), prepared on behalf of the Canadian Radio-Television and Telecommunications Commission, December 1992. *ISDN Has Come of Age*, (with Lee L. Selwyn), prepared on behalf of Prodigy Services Company, November 1992.

A Roadmap to the Information Age: Defining a Rational Telecommunications Plan for Connecticut, (with Lee L. Selwyn, Susan M. Baldwin, JoAnn S. Hanson, David N. Townsend and Scott C. Lundquist), prepared on behalf of the Connecticut Office of Consumer Counsel, October 30, 1992.

Migration Plan for Residential ISDN Deployment, (with Lee L. Selwyn) prepared on behalf of the Communications Policy Forum, Electronic Frontier Foundation, April 20, 1992.

Efficient Pricing for ONA Access : Recommendations for Modifications to Part 69 of the FCC's Rules to Accommodate an Open Network Architecture, (with Lee L. Selwyn, JoAnn S. Hanson, and David N. Townsend), prepared on behalf of the Coalition of Open Network Architecture Parties, The ONA Users Group, and Ad Hoc Telecommunications Users Committee, August 10, 1989.

Use of Featured Group Carrier Switched Access Services for National Paging Access: An Examination of Potential Feasibility, (with Lee L. Selwyn) prepared on behalf of National Satellite Paging, Inc., March 15, 1989.